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In The

Supreme Court of the United States

OCTOBER TERM, 1959

NO. 21

BANK OF AMERICA NATIONAL TRUST AND SAVINGS ASSOCIATION, Petitioner

v.

GILBERT S. PARNELL, Respondent

NO. 22

BANK OF AMERICA NATIONAL TRUST AND SAVINGS ASSOCIATION, Petitioner

v.

FIRST NATIONAL BANK IN INDIANA, Respondent

On Writs of Certiorari to the United States Court of Appeals for the Third Circuit

REPLY BRIEF FOR PETITIONER

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REPLY BRIEF FOR PETITIONER

This reply brief is addressed both to the brief filed on behalf of the defendant-respondent Parnell (referred to herein as "Parnell's Brief") and the brief filed on behalf of the defendant-respondent First National Bank in Indiana (referred to herein as "Bank's Brief").

Before proceeding further, it will be helpful to focus attention on the precise issue in the case. In his charge

to the jury, the trial court dealt with the question of burden of proof (R. 422), saying that—

> "if you find in this case that the plaintiff owned these bonds, that they were stolen from it—then the burden of proof so far as this plaintiff is concerned is to show that fact, that these bonds were owned by it, that they were lost by it in the manner as shown by its evidence. Then the two defendants, Parnell and the bank, not claiming to be owners for value, but as conduits for redemption, must come forward and they then have the burden of showing that they acted innocently, honestly, and in good faith."

Acting under this charge, the jury found a verdict against both respondents. (R. 439.) The jury must, therefore, have found that the defendants failed to meet the burden which was on them to show that they acted "innocently, honestly, and in good faith." (R. 422.)[1]

[1] In reaching this conclusion, the jury may have taken into account (a) that the defendant Rocco was not called by either respondent and even when called by petitioner was not cross-examined by either respondent (R. 493); (b) that, according to the testimony of Rocco, the defendant Parnell (a director of the defendant bank) received as his share of the proceeds of the bonds, five or six thousand dollars (R. 488) and not merely $650 as a retainer and fee for legal services as Parnell testified (R. 317-318); and (c) that despite the amounts involved, over $57,000 in the two transactions here in suit and in excess of $25,000 in an earlier third transaction (R. 478), Parnell received and disbursed the proceeds in $100 bills, and some smaller bills, there being no written records of the transactions except cashier's checks which Parnell endorsed and the bank immediately cashed. (R. 316-319, 344.) Reference is made also to the additional material set forth at pp. 4-5 of our main brief.

Before the respondents can prevail, they must establish two propositions. These are (1) that the question of the correctness of the court's charge on this point is governed by federal and not state law, and (2) that if the matter is one of federal law, the source of that law is to be found in decisions of this Court made many years ago before the enactment of the Negotiable Instruments Law.

These questions are discussed at length in our main brief. This reply brief is confined to answering certain arguments advanced by one or both of the respondents, to pointing out that certain collateral arguments are contrary to fundamental principles of law, and to correcting erroneous statements of matters of record.

I.

The Application of "Federal" Law in Determining the Liabilities of the Respondents Is Not Required or Called for by Any Statute or Regulation.

The respondent bank is a "member bank" of the Federal Reserve System. Great significance is attached to this fact in the brief filed on behalf of the respondent bank. In the Counter Statement of Questions Presented, the first question is phrased: "Can a member bank of the Federal Reserve System be held liable for conversion * * *?" (Bank's Brief 1.) And the second question is put: "Is Federal law applicable to determine the duties, rights and liabilities of parties in transactions involving Home Owners Loan Corporation Bonds * * * issued under Act of Congress authorizing Treasury regulations

concerning the redemption or collection thereof by member banks of the Federal Reserve System?" (Bank's Brief 2.)

Is there anything in any statute or regulation which permits the argument that Congress has preempted the field or indicated an intention that federal law is to govern the liabilities of the parties here? The statutes and regulations on which the respondent bank relies are all set forth under Point I (Bank's Brief 12-14) and in the Appendix (Bank's Brief 41-43) of its brief. The sole reference to a "member bank" is in Treasury Department Circular No. 666, quoted at page 14 of the Bank's Brief, where it is provided that "A Federal Reserve Bank, upon appropriate request, may make payment to a member bank from which bearer securities are received by crediting the amount in the member bank's account." The scope and effect of this provision seem crystal clear. It gives to the several Federal Reserve Banks the right to effect payment by a credit advice, instead of by cash payment or the delivery of a check, if the person presenting the bond so requests and is a member bank and, therefore, one to whom payment can be made by that method. We submit that the statutes and regulations set out in the Bank's Brief prove only the correctness of the statements in our original brief, at page 25, where we said:

> "The only statute relating to the bonds authorizes their issue and is completely silent as to the rights of owners and transferees, except that it is provided that the bonds are to be free of certain taxes. The United States Treasury Department Regulations are

equally silent so far as the rights of owners and transferees are concerned."

It is noted that the opinion of the court below does not seek in any way to support its conclusion on the basis of anything contained in any federal statute or regulation. We think that no such argument can be made and that it is idle to contend otherwise. The sole issue in the case at bar is whether the fact that property alleged to have been converted consisted of securities issued or guaranteed by the United States is sufficient, in and of itself, to require that the liabilities of the parties in the case at bar be determined in accordance with federal law. For the reasons set forth under point I of our original brief, we think that it is not sufficient. Supplementing the discussion in the original brief, and particularly the discussion at pages 18-20, we would refer to *Provident Savings Life Assurance Society v. Ford,* 114 U.S. 635, where it was argued that a suit on a judgment entered in a federal court was a suit arising under the laws of the United States. In answer to this argument, Mr. Justice Bradley replied at 114 U.S. 641-2:

> "What is a judgment, but a security of record showing a debt due from one person to another? It is as much a mere security as a treasury note, or a bond of the United States. If A brings an action against B, trover or otherwise, for the withholding of such securities, it is not therefore a case arising under the laws of the United States, although the whole value of the securities depends upon the fact of their being the obligations of the United States. So if A have title to land by patent of the United States and brings an action against B for trespass

> or waste, committed by cutting timber, or by mining and carrying away precious ores, or the like, it is not therefore a case arising under the laws of the United States. It is simply the case of an ordinary right of property sought to be enforced."

In the absence of any trace of any indication by Congress that this is a matter which should be governed by a special federal rule, no reason is seen why this Court should undertake to prescribe such a rule. This is a federal nation, in which substantial functions are assigned to the States. One of the clearest of these is the regulation of the rights of property between private parties, especially in situations where no interest of the federal government is involved. To say, in the absence of any legislative intimation, that such a matter is governed by a federal rule would be to make new law where none is called for, and would be an interference with the traditional scope of action by the States which might be legitimately questioned. Congress has not called for uniformity and it is hardly the function of the Court to occupy the field.

In Parnell's Brief, it is argued (p. 39) that there must be a uniform federal rule with respect to transfers of government bonds because the rule leaving this matter to state law "would practically transform the nature of bearer obligations into instruments passing by endorsement," and "would completely destroy the usefulness of government bearer bonds as a readily circulating liquid medium of investment. . . ." "Bearer bonds," we are told (Parnell's Brief 40), "as we have known them in the past, would be eliminated from the picture.

The Treasury would be limited to issuance of securities having the characteristic features of registered or non-transferable bonds."

The exaggerated nature of this argument is patent. If arguments against it are needed, they may be summarily stated as follows: (1) Nothing of the sort has happened over the past many years when it has surely not been clearly established that these matters are governed by a uniform federal rule. (2) All of the States have and maintain the rules of "bona fide purchase" and "holder in due course." All that need be done by the purchaser or person dealing with government bonds is to show that he handled them "innocently, honestly, and in good faith." (R. 422.) (3) Congress can apparently control the situation if it should ever conclude, as it has not, that action on its part is necessary. (4) Moreover, the interest and concern of the federal government works both ways. Persons who subscribe to bonds, or who purchase them on the market, will be more interested in doing so if they have a reasonable assurance that they will not lose their title to their bonds by anything short of a genuine bona fide purchase.

In short: Congress has not indicated any desire that transactions in government bonds between private parties should be governed by a uniform federally prescribed rule, and no reason is advanced why such a rule would be advantageous or desirable. On the contrary, the establishment of a federal rule on this matter would be an entry into an area which has been traditionally left to the States in our Federal system of government; such an interference with the States' sphere of action

should not be undertaken by the Court on its own motion, when Congress has not spoken.

It is noted that *United States v. Kramel,* cited at page 19 of the petitioner's brief, is now reported in 234 F. 2d 577.

II.

It Is Wholly Immaterial Whether the Defendants Acted as "Agents" or "Conduits," or as "Purchasers."

It is argued, in one form or another, throughout the brief filed on behalf of the respondent bank that it was not liable because it acted in the transaction not as a "purchaser," but only as an "agent" or "conduit." The same argument is advanced in point II of the brief filed on behalf of the respondent Parnell, but in that brief the thrust of the argument is entirely different. It is said (Parnell's Brief 38) that "Assuming that federal law governs the process of transmitting government bearer bonds through the channels of the Federal Reserve System," the defendant Parnell was but an intermediary in that process and, therefore, may not be charged with liability on the theory that he was a "purchaser" of the bonds.

We think it makes no difference whatever whether Mr. Parnell and the respondent bank are considered as "agents" or "conduits," or as purchasers." We have never contended, as respondent bank asserts (Bank's Brief 15), that liability attached to either defendant because it was "a holder in due course or purchaser." What we have argued, as we think rather clear from our brief, is that the defendants may not escape liability on the ground that either of them was "a holder in due

course." The issue in this case is whether the defendants acted innocently and in good faith. If they did, they are not liable whether they acted as purchasers or as agents only. All this, we think, is very clear on the basis of fundamental law under all the authorities, including those cited by the respondents.

The settled law is as stated in *Morissette v. United States,* 342 U.S. 246, where Mr. Justice Jackson said, at page 270:

> "In the civil tort, except for recovery of exemplary damages, the defendant's knowledge, intent, motive, mistake, and good faith are generally irrelevant. If one takes property which turns out to belong to another, his innocent intent will not shield him from making restitution or indemnity, for his well-meaning may not be allowed to deprive another of his own."

An agent is not exempt from liability for conversion. At common law and apart from the protection afforded by the law of negotiable instruments, an agent who disposes of goods or chattels on behalf of a principal who has no title to the goods is liable to the rightful owner. It matters not in the slightest that he acted only as an agent. To use the words of Mr. Justice Holmes:

> "If an auctioneer in the most perfect good faith, and in the regular course of his business, sells goods sent to his rooms for the purpose of being sold, he may be compelled to pay their full value if a third person turns out to be the owner, although he has paid over the proceeds, and has no means of obtaining indemnity." Holmes, *"The Common Law,"* page 83.

Modern law has made this exception, and it is the exception and not the general rule as one would suppose from the briefs of the respondents, that an agent is not liable if the property dealt with by the agent consists of current money or a negotiable instrument, where the transferee becomes a holder in due course and the agent has acted innocently and in good faith. In other words, the rule of strict liability gives way to the extent of the protection afforded by the law of negotiable instruments, whether statutory or otherwise. The pertinent law as it exists today is correctly and exactly stated in the *Restatement, Torts,* 1948 Supplement, §233:

> "§233. CONVERSION BY DISPOSITION BY AGENT OR SERVANT AS AGAINST ONE OTHER THAN BAILOR.
>
> (1) Except as stated in Subsection (2), one who as agent or servant of a third person disposes of a chattel to one not entitled to its immediate possession in consummation of a transaction negotioted by the agent or servant is liable for a conversion to another who, as against his principal or master, is entitled to the immediate possession of the chattel.
>
> (2) The statement in Subsection (1) is not applicable to an agent or servant who disposes of current money or a document negotiable by common law or by statute pursuant to a transaction by which the transferee becomes a holder in due course of such money or document, unless the agent or servant knows or has reason to know that his principal or master does not have authority so to dispose thereof."

The Comment on Subsection (2) is, in part, as follows:

"Comment on Subsection (2):

c. Negotiable instruments. The statement in Subsection (1) is not applicable to an innocent agent or servant who transfers current money, or, whether by endorsement or delivery, a document negotiable by common law or by statute under circumstances which make the transferee a holder in due course thereof. If, however, the agent or servant at the time of such disposition knows or has reason to know that his principal or master is not authorized so to dispose of the money or document, such agent or servant is liable to the person entitled to the immediate possession thereof.

d. The statement in this Subsection is applicable only when the transferee received the instrument under circumstances which make him a holder in due course. If, for any reason, the transferee fails to obtain title to the instrument, the agent or servant who negotiates it either by endorsement or delivery is liable to the person entitled to the immediate possession of the instrument for its conversion."

The *Restatement, Agency,* §349 is in accord.

There is not the slightest doubt about the law of Pennsylvania. *Lindsley v. First National Bank of Philadelphia,* 325 Pa. 393, 190 Atl. 876 (1937), was an action against a bank to recover the aggregate of sixty-five checks deposited with the defendant bank, which had collected them and paid the amount of the checks to its depositor. The checks bore forged endorsements. It was held that the bank had converted the plaintiff's prop-

erty and the fact that it had acted only as a collecting bank was no defense. The court said at page 397:

> "But in receiving a check for collection, the collecting bank gets no title to the check if the holder depositing it had none; by collecting it, and crediting the collection to the depositor, the bank necessarily assumes dominion over it inconsistent with the payee's control over his own property; this is conversion."

Gruntal v. United States Fidelity & Guaranty Co., 254 N.Y. 468, 173 N.E. 682 (1930), upon which both respondents rely and which is quoted extensively at page 29 of the Bank's Brief, is not contrary to these fundamental principles of law, but in full accord. It was held in that case that an agent who had acted *innocently and in good faith* in disposing of negotiable securities was not liable. The crucial matter was his good faith. The very extract quoted at page 29 of the Bank's Brief leaves no doubt on that score. Quoting from an earlier Massachusetts decision, the court said:

> "The question for decision therefore is whether the defendants who received and sold the bonds and accounted for the proceeds to the apparent owner, *without notice of any infirmity in the title, or of any circumstances which should have put them upon inquiry,* can be held responsible in damages by the true owner for conversion." [Emphasis supplied.]

But in the case at bar the whole matter to be decided is whether the so-called "agents" did act "without notice of any infirmity in the title, or of any circumstances which should have put them upon inquiry".

There is nothing in the opinion, or in the result, in *First National Bank of Blairstown v. Goldberg,* 340 Pa. 337, 17 A. 2d 377 (1941), to support the argument (Bank's Brief 31) that under the law of Pennsylvania the burden of proof in this case rested on the petitioner. Again, as in the *Gruntal* case, there was no question as to innocence and good faith. The question was whether one who acted only as an agent could escape liability for conversion. The question is stated in the opening paragraph of the opinion, 340 Pa. 338:

> "There is a singular dearth of authority in regard to the principal question involved in this case, which is whether a person who, as agent, assists another in the sale of stolen negotiable bonds, but turns over all the proceeds to his principal and acts throughout the transaction innocently and in good faith, is liable for conversion of the bonds in an action by the owner."

The fact that a judgment notwithstanding the verdict in the *Goldberg* case was affirmed affords no basis for an argument that under Pennsylvania law the burden of proof rested on petitioner in the case at bar. The cases cited at page 36 of our original brief show that burden did not rest on the petitioner, and the *Goldberg* case recognizes this. We quote from the opinion, 340 Pa. 340:

> "It was incumbent upon plaintiff to prove only its ownership and loss of the bonds, and the burden would then have shifted to defendants to show that they came into possession of the securities under such circumstances as to relieve them from liability for a conversion. Plaintiff, however, itself presented all of the facts through cross-examination of Gold-

berg, and is bound by his testimony, there being no contradiction of it: *Krell v. Jacobson,* 314 Pa. 522, 527, 172 A. 697, 699. From that testimony no inference of bad faith on the part of either defendant can be drawn."

There is no doubt as to the *Pennsylvania* rule with respect to the burden of proof. Not only the District Judge, and the minority in the court below, but the majority also would seem to agree. The action of the majority in the court below was predicated solely on the applicability of *federal* law. No other basis is discussed, and it is expressly stated (R. 497): "The appellants urge that federal law, under which they claim significantly different results would be reached, should have governed the case." And again (R. 499): "Under federal law, we think the established rule is as appellants say."

It is obvious, of course, from what has been said that it is wholly immaterial whether or not the respondents are termed "holders" as that term is defined in the Negotiable Instruments Law. If they choose not to assert the defense of being "holders in due course", that is their privilege. In the interest of a logical development of the case, we would point out however that the term "holder" as defined in the Negotiable Instruments Law is not the equivalent of "purchaser". The term "holder" is basic to the framework of the Negotiable Instruments Law and is defined in that law as follows:

" 'Holder' means the payee or indorsee of a bill or note, who is in possession of it, or the bearer thereof." (Section 191 of the Pennsylvania Negotiable Instruments Act of May 16, 1901, P.L. 194, Purdon's Pa. Stat. Ann. Tit. 56, §492 (1930).)

Since the respondents were admittedly in possession of a bearer instrument, each was a "holder" within the clear terms of the definition. If authority in addition to the plain words of the statute is required, we cite *McKinley v. Wainstein,* 81 Pa. Super. Ct. 596 (1923), where it is held that the indorsee of a check who took the check for collection was a "holder" and therefore entitled to sue in his own name under Section 51 of the Negotiable Instruments Law.

III.

The Exhibits Said to Have Been Improperly Admitted in Evidence During the Trial Were Admissible on the Basis of the Record.

It is argued in Point V (Bank's Brief 32-6) that certain exhibits (Petitioner's Exhibits 7, 8, 9 and 10) were admitted in evidence on "the assumption that knowledge of their contents would be proven to have reached defendant bank", that such evidence was not given and, therefore, that the trial court erred in not striking the exhibits from the record. This argument is without merit because the record shows so clearly as to leave no doubt whatever that the facts of record are not as the respondent bank says.

The record shows that the trial court refused, throughout the trial, to admit Exhibits 7, 8 or 9 generally or for the purpose of showing notice to the respondent bank. As to all defendants other than the Federal Reserve Bank of Cleveland[1], the trial court admitted the exhibits for the limited purpose of nega-

[1] These exhibits and Exhibit 10 were all taken from the files of the Federal Reserve Bank and were admitted while it was a defendant and generally as to it. (R. 94-95, 99, 105, 114.)

tiving the proposition[9] that the bonds left petitioner's bank in the ordinary course of business. It specifically refused to admit them as any evidence of notice to the respondent bank in the absence of evidence that the exhibits had come, or might reasonably be inferred to have come, to the respondent bank. This was explained by the trial judge on at least three occasions and so clearly as to not permit an argument that he was in any way misled or confused (R. 102-3, 113-14, 133-134). We think it unfortunate, if not somewhat unfair, that, by the isolated sentences quoted at pages 33-34 of the respondent Bank's Brief, it is argued otherwise.

The situation with respect to Exhibit 10, as disclosed by the record, only emphasizes what we have said as to the clear understanding of the trial judge with regard to the admissibility of the four exhibits in question. Exhibit 10 was a circular, dated May 20, 1944, put out by the Pittsburgh office of the Federal Bureau of Investigation. It was addressed to "All Banks and Security Brokers" and the circular is attached in the record at page 453. When the circular was first offered, the trial court refused to admit it in evidence in the absence of testimony from the Federal Bureau of Investigation as to where it was sent (R. 128-130). To avoid any possible prejudice to the other defendants, counsel for petitioner agreed not to offer the circular even against the Federal Reserve Bank at that time, but to place upon the record a stipulation to the effect

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[9] The questions repeatedly put to plaintiff's witness Britton on cross-examination could well create the impression that the bonds had not been stolen, but had been misplaced only, or taken by an employee of petitioner. (R. 64-82.)

that the Federal Reserve Bank had received from the Federal Bureau of Investigation a notice of the theft of the bond (R. 142-143). Later during the trial, petitioner subpoenaed the agent in charge of the Pittsburgh office of the Federal Bureau of Investigation, who testified that Indiana, Pennsylvania, was within the geographical area served by the Pittsburgh office and that Mr. H. T. O'Connor, whose name appeared in the circular, had been in charge of the Pittsburgh office in May, 1944, when the circular was issued (R. 189-190). The witness objected to the production of the file of the Federal Bureau of Investigation on the basis of Bureau policy (R. 196). In order to avoid a direct ruling upon the question of the availability of the file, the court suggested that the witness examine the file and report as to whether or not it disclosed anything relative to Exhibit 10, as to whom or when it was sent (R. 200-201). In lieu of producing the file, it was later stipulated what the Federal Bureau of Investigation Agent Hallford would testify if called. The stipulation (R. 249-250) was to the effect that Exhibit 10 had been put out by the Pittsburgh office of the Federal Bureau of Investigation at the request of the Los Angeles office of the same organization, and that the file disclosed that subsequent to the mailing of the circular the Pittsburgh office had by letter advised the Los Angeles office "that the circular had been mailed to all banks and security brokers in the Pittsburgh district" (R. 249-250). After this evidence of the mailing of Exhibit 10, the exhibit was admitted in evidence as to the respondent bank and the Federal Reserve Bank of Cleveland (R. 250).

We think that all four exhibits were admissible as evidence of notice, but as Judge Goodrich has so succinctly said (R. 515): "we need not decide this" on this record.

Conclusion.

The collateral questions raised by the respondents are clearly without merit. They were not relied on in any way by the majority below, and the minority opinion expressly states that "there is no merit in them and they do not require discussion." (R. 516.)

When these matters are cleared away it is apparent that the sole issue in the case is the one passed upon by the Court below, namely, whether the question of the burden of proof of good faith is a matter to be decided in accordance with the law of Pennsylvania where the transactions occurred, or is one to be governed by some sort of federal law, though no rule of any sort has been prescribed by Congress.

For the reasons stated in our principal brief and supplemented here, we submit that the question of burden of proof of good faith in this case was properly submitted to the jury in accordance with the established law of Pennsylvania. Accordingly, the judgments of the Court of Appeals should be reversed and the judgments of the District Court affirmed.

Respectfully submitted,

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October 1956.